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JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

NO. 30B
August 15, 1986

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Update On Financial Liberalization In Japan

Although Tokyo listed only one step toward financial liberalization in its report on implementing the 1985 action program (see article in this issue), the Ministry of Finance continues to make incremental changes in financial rules and regulations. The cumulative impact of these changes cannot be ignored, especially since U.S. debt financing needs have not diminished and the value of the yen has continued to rise gradually against the dollar.

MOF announced a new round of moves July 19 to liberalize interest rates paid on deposits. Effective September 1 the minimum time deposit on which market-determined interest rates will be paid will be lowered from Y500 million ($3.1 million at Y160=$1.00) to Y300 million ($1.9 million). As part of its financial reform program, Tokyo agreed in 1984 to liberalize interest rates. Free-market rates on large deposits were initiated October 1, 1985, with large defined as a minimum of Y1 billion ($6.3 million). MOF dropped this floor for

No Turnaround Likely In U.S. Trade Deficit Until 1987

Eighteen months after the dollar peaked on foreign exchange markets there are still few signs that the quarterly U.S. trade deficit has bottomed out (see Table 1). While Reagan administration trade policymakers and business economists alike had warned that a turnaround would take time because of the perverse initial impact of the dollar's depreciation (the J-curve effect), past experience indicated that at the outside, the weaker dollar should begin to influence trade flows no later than 1986's second half. With imports (c.i.f.) outrunning exports at an annual rate of $167.8 billion at mid-year, however, analysts are now predicting that the trade deficit, which ballooned to $148.5 billion in 1985, will not contract until 1987 at the earliest.

Why the backpedaling? The reasons are starting to have a familiar ring. Although the dollar has plunged in value against Japan's yen and the currencies of West Germany, the United Kingdom, France and Italy over the last 18 months, it has held its ground or even appreciated against the currencies of the other five countries that make up the list of the top ten U.S. trading partners. The dollar is up roughly 2.5 percent against the currency of Canada, the biggest U.S. export market and the number-two import supplier behind Japan, and by a huge margin against the currency of Mexico, the third-largest U.S. trading partner. And with the Taiwanese dollar, Korean won and Hong Kong dollar moving in synch with this country's dollar, another 6 percent or so of U.S. exports and 10 percent-plus of U.S. imports remain unaffected by the dollar's depreciation.

What's more, the benefits of the lower dollar have not yet shown up in the U.S. trade results with Japan and Europe (see Table 2). Slow growth abroad continues to put a damper on demand for American-supplied manufactures and industrial and agricultural inputs. At the same time, Japanese and European manufacturers are in no rush to hike prices on their U.S.-bound exports, having decided to sacrifice short-term profits for market share. The money foreign competitors earned in the American market by not cutting export prices during the period of the strong dollar gives them the flexibility to pursue this sales strategy. Moreover, the declining dollar plus the fall in world oil prices gives Japanese and European producers some help on the cost side.

At first glance the data on trade with Japan through June (see Table 3) would seem to undermine the argument that the weaker dollar has had no impact on U.S. export and import numbers. After all, sales to Japan were up 13.2 percent to $13.1 billion after slipping 0.3 percent in 1985's first half. But a closer look at the export figures (see Table 4) reveals that all of this gain and then some resulted from transshipments of foreign gold through the United States to Japan. Adjusting for these shipments, exports were off by a bigger margin in the first six months of 1986 than in the year-earlier period.

The slowdown in the expansion of imports from Japan is similarly deceptive. Most of the cutback in the growth rate from 25.2 percent in the first half of 1985 to 16.7 percent this year reflected a big drop in arrivals of steel mill products as a result of the administration's import restraint program. A few other big-ticket items were in the minus column (see Table 5), but gainers outnumbered losers by a huge margin. More significantly, larger volume played a bigger role in the advance of imports to $41.8 billion (c.i.f.) than higher prices, a quick survey of major products indicates. The one exception was cars, which jumped 31.4 percent to $9.8 billion on a 9.7 percent shipment

Table 1: Total U.S. Trade

(in millions of dollars)

	Exports (f.a.s.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985: I	$56,146	4.4%	$87,521	5.6%	$-31,375
1985: II	54,322	-1.1	92,216	9.1	-37,894
1985: III	50,345	-5.5	88,683	-2.3	-38,338
1985: IV	52,333	-6.4	93,207	12.4	-40,874
1986: I	53,654	-4.4	97,125	11.0	-43,471
1986: II	54,465	0.3	94,914	2.9	-40,449

Table 2: U.S. Trade Balance With Top Ten Trading Partners

(in millions of dollars; exports, f.a.s., imports, c.i.f.)

	1985	January-June 1985	January-June 1986
Total	$-148,480	$-69,268	$-83,921
1. Canada	-22,176	-10,523	-11,775
2. Japan	-49,749	-24,235	-28,702
3. Mexico	-5,757	-2,629	-2,513
4. West Germany	-12,182	-5,798	-7,709
5. United Kingdom	-4,300	-1,127	-2,322
6. Taiwan	-13,061	-6,511	-7,077
7. Korea	-4,757	-1,909	-3,082
8. France	-3,864	-1,943	-1,857
9. Italy	-5,756	-2,481	-3,075
10. Hong Kong	-6,208	-2,661	-2,771

Table 3: U.S. Trade With Japan

(in millions of dollars)

	Exports (f.a.s.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1985: I	$6,252	9.8%	$17,373	26.4%	$-11,121
1985: II	5,298	-10.1	18,413	24.1	-13,115
1985: III	5,514	-5.5	18,216	5.9	-12,702
1985: IV	5,567	-9.6	18,379	25.9	-12,812
1986: I	5,574	-10.8	20,888	20.2	-15,315
1986: II	7,499	41.5	20,886	13.4	-13,387

Table 4: U.S. Exports to Japan

(in millions of dollars, f.a.s. value basis)

	January-June 1985	January-June 1986	Percent Change
Total Exports	$11,550.1	$13,072.2	13.2%
Industrial Supplies	4,449.5	4,122.0	-7.4
Bituminous Coal	418.7	325.4	-22.3
Petroleum Products	392.8	280.6	-28.6
Natural Gas	115.0	98.7	-14.2
Nuclear Fuels	55.9	23.8	-57.4
Logs and Lumber	430.8	493.3	14.5
Paper Base Stocks	242.8	254.9	5.0
Paper and Paper Products	140.5	166.8	18.7
Organic Chemicals	354.3	371.4	4.8
Inorganic Chemicals	401.8	394.5	-1.8
Plastics and Synthetic Resin Compounds	156.7	155.9	-0.5
Manufactured Fertilizers and Insecticides	113.0	138.7	22.7
Steel Scrap	97.2	124.4	28.0
Nonferrous Ores and Scrap	227.7	241.9	6.2
Nonferrous Metals	167.2	104.8	-37.3
Textiles	61.3	57.8	-5.7
Raw Cotton	269.3	96.3	-64.2
Hides and Skins	136.4	164.0	20.2
Leaf Tobacco	83.4	74.0	-11.3
Capital Goods	3,223.0	3,022.0	-6.2
Nonelectric Machinery	1,828.8	1,689.5	-7.6
Data Processing Equipment	731.3	656.7	-10.2
Measuring, Testing and Control Instruments	244.8	220.7	-9.8
Laboratory Testing and Control Instruments	57.4	49.4	-13.9
Scientific, Professional and Medical Equipment	138.3	156.6	13.2
Power Generating Equipment (excl. aircraft and automotive engines)	40.5	37.7	-6.9
Metalworking Equipment	56.3	76.1	35.2
Service Industry Equipment	61.1	65.8	7.7
Electric Machinery	433.9	436.9	0.7
Generators and Transformers	37.5	38.0	1.3
Broadcast and Communications Equipment	179.0	180.6	0.9
Telephonic and Other Electric Equipment	217.5	218.3	0.4
Transportation Equipment	960.3	895.6	-6.7
Civilian Aircraft	542.0	410.1	-24.3
Civilian Aircraft Engines and Parts	276.7	309.1	11.7
Automotive Parts	98.1	109.6	11.7
Food and Feed	2,306.6	2,344.3	1.6
Corn	686.0	475.2	-30.7
Sorghum	105.4	78.1	-25.9
Soybeans	466.1	447.6	-4.0
Wheat	226.8	231.3	2.0

Fruits and Vegetables	244.4	287.5	17.6
Meat and Meat Products	255.6	351.1	37.4
Fish and Fish Products	145.3	232.7	60.2
Consumer Goods	737.8	790.3	7.1
Pharmaceuticals	310.4	327.2	5.4
Toys and Sporting Goods	43.4	44.2	1.8
Cigarettes	40.3	53.0	31.5

Table 5: U.S. Imports from Japan

(in millions of dollars, Customs value basis)

	January-June 1985	January-June 1986	Percent Change
Total Imports	$33,967.8	$39,960.1	17.6%
Automotive Products	11,743.6	15,728.3	33.9
Cars	7,488.3	9,837.0	31.4
Trucks	2,084.3	2,868.2	37.6
Automotive Parts	2,166.7	3,015.4	39.2
Capital Goods	10,967.8	12,332.0	12.4
Nonelectric Machinery	7,418.1	8,365.9	12.8
Business Machines	3,303.1	3,734.3	13.1
Metalworking Machinery	630.9	665.1	5.4
Agricultural Machinery	192.4	266.7	38.6
Specialized Industrial Machinery	631.7	763.8	20.9
Scientific, Professional and Medical Equipment	292.3	409.4	40.1
Electric Machinery	3,375.4	3,688.5	9.3
Transportation Equipment	174.3	277.6	59.3
Consumer Goods	6,908.5	7,644.2	10.6
Video and Audio Recorders and Players and Stereo Equipment	2,662.3	2,930.2	10.1
Television Sets	376.4	447.4	18.9
Radio Receivers	157.9	119.5	-24.3
Tableware and Glassware	206.9	218.8	5.8
Metal Cookware and Cutlery	190.1	224.7	18.2
Photographic and Optical Goods	470.0	545.2	16.0
Clocks and Watches	230.3	226.4	-1.7
Toys and Sporting Goods	264.9	246.4	-7.0
Motorcycles and Parts	472.0	519.3	10.0
Clothing	238.0	234.9	-1.3
Intermediate Goods	3,752.4	3,610.8	-3.8
Steel Mill Products	1,731.6	1,270.3	-26.6
Nonferrous Metals	263.3	264.9	0.6
Organic Chemicals	298.3	361.3	21.1
Textiles	358.7	438.3	22.2

gain to 1.3 million vehicles. Otherwise, the relationship held. Trucks, for example, were up 29.6 percent in volume to 515,400 units and 37.6 percent in value to $2.9 billion, while a 7.5 percent rise in deliveries of video cassette recorders to 8.4 million units translated into a sales gain of just 2 percent to $2.1 billion.

Susan MacKnight

Notes

• Amid renewed charges from U.S. steel industry executives and congressional steel caucus members that President Reagan's September 1984 plan to contain the market inroads of foreign steel is a flop, Japan has agreed to cut 1986 U.S.-bound steel exports as compensation for exceeding its quota during the first 15 months of the restraint program. Under an arrangement finally hammered out July 20 by the Commerce Department and the Ministry of International Trade and Industry, Japan will "pay back" the overshipments by reducing this year's ceiling on exports of finished steel (sheet and strip, plate, structural shapes, bars, pipe and tubing, and wire and wire rod) plus fabricated structural products and semi-finished steel to 4.1 million metric tons from an originally projected 4.6 million metric tons. Nearly half of the cutback fell on pipe and tubing; the quota on these products dropped by 245,000 metric tons to 438,000 metric tons. Roughly 117,000 metric tons were deducted from the restraint level for structural shapes, reducing it to 572,000 metric tons, while the limit on sheet and strip was trimmed by 103,000 metric tons to 2,377,000 metric tons. Small adjustments were made in the quotas on wire and wire rod (373,000 metric tons for 1986), bars (180,000 metric tons), and plate (16,000 metric tons) as well as in the shipment caps on welded H beams and other fabricated structural products (101,000 metric tons) and semi-finished steel (62,000 metric tons).

With an already long list of outstanding bilateral trade problems, Tokyo did not want the overshipment issue to turn steel into the latest U.S.-Japan dispute. At the same time, though, MITI officials were reluctant to bow to U.S. demands for an offset in 1986 exports since they are convinced that Japanese steel mills have been unfairly forced to shoulder the brunt of the Reagan administration's crackdown on steel imports. Ministry spokesmen have long complained that although Japan agreed in March 1985 to a five-year cap on shipments retroactive to October 1984 (see JEI Report No. 11B, March 22, 1985), the European Community avoided renegotiating its 1982 export-restraint arrangement with the United States until November 1985 and then held out for a January 1, 1986 starting date. They are equally irked by the fact that Japan agreed to reduce its target share of U.S. finished steel consumption to 5.8 percent from a five-year average of 6.3 percent, while the EC's market participation was trimmed by just 0.1 percentage point to 5.6 percent. The fact that Canadian steel remains unregulated is another sore point, especially since Canada's market share continues to edge up.

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The views expressed in this report are those of the authors and do not necessarily reflect those of the Japan Economic Institute.